

Teacher Lesson Plan

Module 3: Interest Income

Time Frame

One to two class periods

Curriculum Area(s)

- Technology
- Civics/Government
- Family and Consumer Sciences
- History/Social Studies
- Economics

Purpose

To help students understand that most interest income is taxable

Objectives

Students will be able to

- identify taxable interest income.
- report taxable and tax-exempt interest income.

Materials

Online

Student Lesson—Interest Income

Tax Tutorial—Interest Income

Simulation 3—Using Your W-2 and Form 1099-INT to File Your 1040EZ

Assessment—Interest Income

Assessment Solutions—Interest Income

Print (PDF)

Fact Sheet—Interest Income

Teacher Lesson Plan—Interest Income

Tax Forms

Form W-2, Wage and Tax Statement

Form 1099-INT, Interest Income

Form 1040EZ, Income Tax Return for Single and Joint Filers with No Dependents

Background

Interest is the charge for the use of borrowed money. A common way to earn interest income is to deposit funds in a financial institution, such as a bank or credit union. Most interest income is taxable—that is, it is subject to income tax. **Tax-exempt interest income** is not subject to income tax and is earned on funds loaned to states, cities, counties, or the District of Columbia. In most cases, interest income is reported on Form 1099-INT. All **taxable interest income** is reported on the taxpayer's return, even if it is not reported on Form 1099-INT.

Key Terms

interest—The charge for the use of borrowed money.

taxable interest income—The income a person receives from certain bank accounts or from lending money to someone else.

tax-exempt interest income—Interest income that is not subject to income tax. Tax-exempt interest income is earned from bonds issued by states, cities, or counties and the District of Columbia.

Opening the Lesson

Hand out Fact Sheet—Interest Income. Use the following questions to prompt students to share what they know about interest:

- What is interest?

Interest is the charge for the use of borrowed money.

- In what situations does a taxpayer earn interest?

when taxpayers place money in a savings account or a certificate of deposit [CD]

- In what situations does a taxpayer owe interest?

when taxpayers borrow money

Then, explain that this lesson focuses on interest income, not interest expense.

Note: Refer students who may want to work independently on this module to Student Lesson—Interest Income.

Developing the Lesson

Direct students to Tax Tutorial—Interest Income, and explain that this tax tutorial focuses on taxable and tax-exempt interest income. Tell students that they will learn how interest income is reported to them and, in turn, how they report interest income on their tax returns. Inform students that they will have an opportunity to look at tax forms associated with interest income.

Online Activity

Direct students to Simulation 3—Using Your W-2 and Form 1099-INT to File Your 1040EZ.

Explain that by using information from Forms W-2 and 1099-INT, they will complete Form 1040EZ for Tasha Mills, a single taxpayer who has no dependents.

Concluding the Lesson

After students have completed Tax Tutorial—Interest Income and Simulation 3—Using Your W-2 and Form 1099-INT to File Your 1040EZ, ask them whether they have questions about interest income or Form 1099-INT. To ensure that they understand the difference between interest income and interest expense, ask the following questions:

- What is an example of when you would pay interest?
car loans, tuition loans, mortgages, credit card debt
- What is an example of when you would earn interest?
when money is loaned to financial institutions or friends

Assessment

As a final review, summarize the major lesson points. Remind students that interest is the charge for the use of borrowed money. Tell them that interest income can be taxable or tax-exempt and that interest income is reported on Form 1099-INT. Finally, explain that all taxable interest income is reported on taxpayer's return, even if it does not appear on Form 1099-INT. When students are comfortable with the material, have them complete Assessment—Interest Income.

Assessment

Module 3: Interest Income

Part 1

Determine whether the interest income is taxable or tax-exempt. Answer the following questions by typing the words *taxable* or *tax-exempt* in the space provided. To assess your answers, click the *Check My Answers* button at the bottom of the page.

1) Interest received on a certificate of deposit (CD) is

taxable

2) Interest received on a bond issued by the state of California to fund school buildings is

tax-exempt

3) Interest received on a loan you made to your business partner is

taxable

4) Interest received on a bond issued by the city of Austin, Texas, for a redevelopment project is

tax-exempt

5) Interest income is considered

A. earned income

B. unearned income *Correct*

Part 2

Review Form 1099-INT for Gloria Sanchez by clicking the button *View Form 1099-INT*. Then, answer the following questions by typing your answers in the space provided. To assess your answers, click the *Check My Answers* button at the bottom of the page.

1) What is the taxpayer's full name?

Gloria Sanchez

2) How much interest income, not including interest on U.S. Savings Bonds and Treasury obligations, did the taxpayer earn?

\$432.87

3) Did the taxpayer earn interest on U.S. Savings Bonds?

A. Yes *Correct*

B. No

4) Which box shows the federal income tax withheld?

box 4

5) Should taxpayers report taxable interest income that does not appear on Form 1099-INT?

A. Yes *Correct*

B. No